

New Issue: Moody's assigns Aaa to \$977.8M of Georgia General Obligation Bonds

Global Credit Research - 12 Jun 2014

Approximately \$9.7B in similar debt outstanding

GEORGIA (STATE OF)
State Governments (including Puerto Rico and US Territories)
GA

Moody's Rating

ISSUE		RATING
General Obligation Refunding Bonds 2014D		Aaa
Sale Amount	\$162,995,000	
Expected Sale Date	06/17/14	
Rating Description	General Obligation	
General Obligation Bonds 2014A		Aaa
Sale Amount	\$649,970,000	
Expected Sale Date	06/17/14	
Rating Description	General Obligation	
General Obligation Bonds 2014B (Federally Taxable)		Aaa
Sale Amount	\$151,115,000	
Expected Sale Date	06/17/14	
Rating Description	General Obligation	
General Obligation Bonds 2014C (Federally Taxable Qualified School Construction Bonds - Direct Pay)		Aaa
Sale Amount	\$13,750,000	
Expected Sale Date	06/17/14	
Rating Description	General Obligation	

Moody's Outlook STA

Opinion

NEW YORK, June 12, 2014 --Moody's Investors Service has assigned a rating of Aaa to the State of Georgia's planned offering of approximately \$977.8 million of general obligation bonds in four series: 2014A tax exempt, 2014B (federally taxable), 2014C (Federally Taxable Qualified School Construction Bonds-Direct Pay) and 2014D refunding bonds. The new money bonds consist of series 2014A (\$649.9 million), 2014B (\$151.1 million), and series 2014C (\$13.7 million). Proceeds of the new-money bonds will fund a variety of state capital projects. The 2014D refunding bonds (\$162.9 million) will provide debt-service savings. The bonds are expected to sell on June 17th.

SUMMARY RATING RATIONALE

The highest-quality rating is supported by Georgia's conservative fiscal management, replenishment of budgetary reserves that were largely used up during the recession, moderate debt burden and signs of growth (albeit slow)

during the current economic recovery. The rating outlook is stable, based on our expectation Georgia will take appropriate steps to maintain balanced financial operations and replenish reserves as the economy recovers.

STRENGTHS

- Conservative fiscal management, including prompt responses to revenue declines
- History of rapid replenishment of budget reserves
- Relatively well-funded pensions

CHALLENGES

- Slower economic growth coming out of the recession
- Above-average unemployment rate
- Large unfunded retiree health benefits liability

DETAILED CREDIT DISCUSSION

RATING REFLECTS FINANCIAL MANAGEMENT PRACTICES

Georgia's Aaa general obligation rating is based on financial management practices enforced by statutory and constitutional provisions that have helped keep financial operations largely balanced and have encouraged strong recovery from previous economic downturns. The state's constitution limits growth in appropriations to net projected revenues from existing sources, plus appropriations from reserves. Projected revenue is determined by the governor, giving the executive strong power to constrain expenditures. A history of prompt spending cuts in response to revenue shortfalls has been an important aspect of the state's credit profile.

FISCAL 2014 YEAR-TO-DATE REVENUES ARE RUNNING AHEAD OF THE AMENDED BUDGET FORECAST

The fiscal 2014 amended budget (passed during the 2014 legislative session) requires general fund revenue growth of 3.4%, an increase of 1% (\$121.4 million) over the enacted fiscal 2014 budget. The state amended the enacted budget to account for slight revenue over-performance early in the year. Year-to-date figures through May for revenues collected by the Department of Revenue show tax revenue up 4.5%, compared to the amended growth target of 3.8%. Tax revenue growth is spread over different categories. Personal income tax and corporate income tax were up by 1.5% (\$118 million) and 16.1% (\$102 million) respectively, while sales tax revenues were down by 3.8% (\$187.9 million), reflecting the elimination of sales tax on automobile sales. The state eliminated this tax during the 2013 legislative session, opting to implement a title ad valorem tax in its place, which is not captured in the sales tax category but is captured in the motor vehicle tag, title, and fee revenue category. As a result, motor vehicle tag, title, and fee revenues are up by 169.5% (\$620.9 million).

The enacted fiscal 2014 budget incorporated a 3% reduction in state agency expenditures. The fiscal 2014 amended budget required no additional cuts to state agency expenditures, marking the first time since the recession that the state didn't have to further reduce expenditures in order to rebalance its budget mid-year. The amended budget incorporated an additional \$130 million for K-12 spending and \$25 million in additional healthcare spending. The state did not rely on any one-time revenue sources in the fiscal 2014 budget and used recurring revenues to cover recurring expenditures, making the fiscal 2014 budget structurally balanced. The state is on track to end fiscal 2014 with a general fund surplus.

FISCAL 2015 ENACTED BUDGET INCORPORATES 4.3% GENERAL FUND REVENUE GROWTH

The fiscal 2015 enacted budget incorporates general fund revenue growth of 4.3% and tax revenue growth of 4.4% over the amended fiscal 2014 budget. No state agency reductions were incorporated in the approved budget. The budget incorporates a substantial increase in K-12 funding of \$514 million (5%), \$87 million for projected growth in Medicaid and the state's kids healthcare program. The enacted fiscal 2014 budget also includes the full annual required contributions to the state retirement systems. The enacted fiscal 2015 budget is balanced with projected revenues expected to fully cover budgeted expenses with no reliance on one-time revenue sources.

STATE HAS BEGUN TO REBUILD BUDGETARY RESERVES AND AVAILABLE FUND BALANCE

Georgia has a history of rebuilding fund balances rapidly as economic conditions allow, primarily by replenishing

its rainy day fund, the Revenue Shortfall Reserve (RSR). By law, the RSR receives any fiscal year-end surplus and can hold as much as 15% of prior-year net revenues. The RSR balance at the end of fiscal 2012 equaled \$380 million (2% of revenues), after the state appropriated \$172.7 million from the RSR for K-12 expenditures during the fiscal 2013 budget year. After positive revenue performance resulting in a surplus and agency lapses in fiscal 2013 the state's RSR balance was \$717 million (4%) at the close of fiscal 2013, after appropriating \$182.9 million for a mid-year, K-12 funding adjustment. Based on current fiscal 2014 revenue trends, we expect RSR replenishment to continue in the current and future fiscal years, which will bolster available balances. Georgia has a somewhat volatile economy, outpacing the nation during expansions and underperforming during contractions. This tendency may help the state exceed budgetary targets and rebuild reserves.

The state's fiscal 2013 comprehensive annual financial report (CAFR) showed an unrestricted, unassigned general fund balance of \$798 million, approximately 4% of state-source revenues in fiscal 2013. The 2013 fund balance reflects a trend of growth from fiscal 2012, when the state had a GAAP unrestricted, unassigned balance of \$334 million. The increase is attributable to better than expected revenue performance in fiscal 2013. GAAP-based available fund balance levels are important indicators of states' financial and governance strength. The state expects to continue its trend of positive fund balances through fiscal 2014.

MODERATE ECONOMIC GROWTH FORECAST

Georgia's recovery from the recession has been at a slightly higher rate than that of the US. Employment growth for the calendar year through April was 1.9%, compared with the nation's 1.7%. The harsh winter was expected to impact 2014 Q1 growth, but the state expects growth to pick up in the second half of the year. The employment gains have been strongest in the construction, leisure and hospitality, and professional and business services. The state's housing sector, which was affected substantially during the downturn, is starting to show signs of improvement. The state's unemployment rate remains above-average, at 7% versus the US rate of 6.3% for April. However, this is an improvement from the high rate of 10.2% in 2010.

PROPOSED ADJUSTMENTS TO THE TAX CODE

During the 2014 legislative session, the senate adopted a resolution to prohibit any increase in the maximum marginal rate of income tax in effect on January 1, 2015. The current maximum marginal rate of income tax is 6%. The resolution calls for an amendment to the state constitution, which would require voter approval in the November general election. If the amendment passes, it will be effective as of January 1, 2015, and would restrain the state's ability to increase revenues in the future.

BOND ISSUANCE GOVERNED BY 1972 CONSTITUTIONAL AMENDMENT

Georgia's debt issuance practices are governed by a 1972 constitutional amendment that authorized the state to issue general obligation and guaranteed revenue bonds. The amendment also created the Georgia State Financing and Investment Commission to oversee state debt issuance. The constitution does not allow debt to cover a revenue shortfall unless it is repaid within the same fiscal year by taxes levied for that year. The state currently issues only general obligation bonds or full faith and credit-guaranteed revenue bonds. In November 2012, voters approved an amendment to the state constitution allowing the Board of Regents and the State Properties Commission on behalf of state agencies to enter into multi-year lease agreements, not to exceed 20 years. Authorization for \$125 million in financing was approved for fiscal 2014, only \$13.5 million of that authorization was initiated.

The state's constitution mandates conservative debt issuance practices by imposing a 25-year maximum term and a maximum annual debt-service cap at 10% of prior-year net revenues. Georgia has minimal exposure to variable-rate debt, with a single issue equal to about 1.3% of total debt outstanding. While Georgia in 2005 passed a law allowing interest rate swaps, it has not entered any swap agreements.

MODERATE DEBT BURDEN

In Moody's 2014 State Debt Medians report, Georgia's debt-per-capita ranked 25th, at \$1,064, compared with the \$1,054 national median for states. Its 2.9% debt-to-income ratio was 22nd, compared with the 2.6% median. Georgia's debt burden is relatively moderate, reflecting GO borrowings for capital projects as well as issuance of \$1.65 billion of grant anticipation notes by the Georgia State Road and Tollway Authority (currently \$1 billion outstanding). These securities, which finance Federal Highway Administration-approved road construction projects, are included in the calculation of tax-supported debt even though pledged revenues come from the federal government, and Georgia itself is not the legal obligor.

UNFUNDED PENSION LIABILITY SLOWLY RISES

Georgia has two multi-employer cost sharing plans, the Employees' Retirement System (ERS) and the Teacher Retirement System (TRS). The reported unfunded pension liabilities for the ERS and TRS amounted to \$4.8 billion and \$13.6 billion, respectively, as of June 30, 2013, up from \$4.5 billion and \$12 billion in 2012.

Based on Georgia's fiscal 2012 pension data, we have calculated that the overall retirement systems' adjusted net pension liability (ANPL) was 36.1% of revenues, below the 50-state median of 63.9%. Other pension ratios such as ANPL to personal income, GDP, and population are similarly below median levels. Moody's adjusted net pension liability applies a bond index rate to determine the present value of plan liabilities, incorporates the market (rather than actuarial) value of plan assets and makes certain other changes to improve comparability of reported pension liabilities. The adjustments are not intended to replace Georgia's reported liability information, but to improve comparability with other rated states. Georgia's share of liability for both pension plans was determined in proportion to its contributions to each plan.

STATE FACES SUBSTANTIAL OPEB LIABILITY, DESPITE RECENT REFORMS

The state enacted legislation in 2009 to create two OPEB funds: one for state employees and one for school personnel. As of June 30, 2012, the state employee OPEB fund had a \$3.8 billion unfunded actuarial accrued liability (UAAL), down from \$4.3 billion, while the school personnel fund's unfunded OPEB liability was \$10.8 billion, down from 11.1 billion. For fiscal 2014, the annual required contribution (or ARC) to both provide for current service and to amortize the liability for past service for the state employee plan was \$321 million, and the ARC for the school personnel plan was \$943 million. On an aggregate basis, these amounts represent about 8% of state revenues. The state is currently not funding the ARC, but operates on a pay-as-you go basis with respect to OPEB. Georgia notes that accounting standards for reporting retiree health benefit liabilities are not funding requirements, and that its OPEB plan funding will remain subject to appropriation and under the control of state agencies.

OUTLOOK

The outlook for Georgia's general obligation credit rating is stable, based on Moody's expectation that the state will maintain balanced financial operations and continue rebuilding financial reserves.

WHAT COULD MAKE THE RATING GO DOWN

- Return to negative fund balances over an extended period
- Economic deterioration leading to revenue declines and lack of budget balance
- Renewed reliance on non-recurring fiscal measures
- Failure to address large, unfunded retiree health benefits liability or substantial deterioration in pension funded status

The principal methodology used in this rating was US States Rating Methodology published in April 2013. Please see the Credit Policy page on www.moody.com for a copy of this methodology.

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